ATTACHMENT 2

STAMP AND RETURN

ORAL ARGUMENT IS SCHEDULED FOR MAY 13, 1997 AT 9:30 AM

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

ILLINOIS PUBLIC TELECOMMUNICATIONS ASSOCIATION, Petitioner, v. FEDERAL COMMUNICATIONS COMMISSION and UNITED STATES OF AMERICA, Respondents, COMPETITIVE TELECOMMUNICATIONS ASSOCIATION, et al., Intervenors.	No. 96-1394 and consolidated cases

Petitions for Review of Orders of the
Federal Communications Commission
CC Docket 96-128

BRIEF FOR PETITIONERS
AMERICAN PUBLIC COMMUNICATIONS COUNCIL, GEORGIA PUBLIC COMMUNICATIONS ASSOCIATION, AND ILLINOIS PUBLIC TELECOMMUNICATIONS ASSOCIATION

February 14, 1997

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A. Discontinuing Payphone Subsidies

Section 276(b)(1)(B) requires the FCC to adopt regulations that "discontinue . . . all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues . . . ." Id. § 276(b)(1)(B). The conference report on the Telecommunications Act of 1996, which adopted the House version of Section 276, stated that to discontinue payphone subsidies "[t]he [Bell company] payphone operations will be transferred, at an appropriate valuation, from the regulated accounts associated with local exchange services to the [Bell company's] unregulated books." See H.R. Conf. Rep. No. 104-458, at 158 (1996) ("Conference Report").

In its rulemaking to implement Section 276, the Commission proposed to "deregulate" the Bell companies' payphone services by requiring a Bell company to remove all payphone-related assets from the regulated rate base. The independent payphone companies urged the Commission also to require that these assets be transferred to unregulated books, in accordance with the Conference Report language, and to require the Bell companies to credit their regulated accounts for the full market value of their payphone operations, including the value of location contracts,[4] goodwill, and other intangibles.[5] California Payphone Association ("CPA") Comments at 16-18; GPCA Comments at 15-16. Otherwise, contrary to the Congressional intent, ratepayers for regulated services would not be repaid for years of subsidies that built the market value of the Bell companies' payphone operations. CPA Reply Comments at 12-15; Peoples Telephone Company, Inc. Reply Comments at 20-21.

The Independents also contended that the emerging competitive payphone marketplace would suffer if the Bell companies' nonregulated payphone divisions could avoid carrying on their books the full value of the transferred payphone assets. The record indicated that the fair market value of a payphone business, considered as a "going concern," is likely to be far in excess of net book cost.[6] Order ¶ 164; Communications Central, Inc., Reply Comments at 14-16, Att. B; GPCA Reply Comments at

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[4] Location contracts are agreements whereby property owners provide space for the installation of payphones in return for a commission or fee.

[5] In other words, the Bell companies' regulated revenue requirements would be reduced by an amount that reflects the net book cost of the transferred assets plus any gain in market value of the transferred assets. Democratic Cent. Comm. v. Washington Metro. Area Transit Comm'n, 485 F.2d 786 (D.C. Cir. 1973), cert. denied, 415 U.S. 935 (1974).

[6] "Net book cost" is the original cost of the physical assets minus accumulated depreciation.

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13-14, Att. 3. In enacting Section 276 to address "the competitive imbalances that exist in the payphone industry" (House Report at 88), the Independents contended, Congress could not have intended to let the Bell companies begin nonregulated operations with the largest single accounting entry -- their location contracts and goodwill -- not even reflected on their balance sheets. Letter from Albert H. Kramer to William F. Caton (Sept. 11, 1996).

The Commission agreed with the Independents that, if the Bell companies' payphone assets were transferred to unregulated books, they must be transferred at the market value of the going concern, including intangibles. Order ¶ 164. However, the Commission then decided that, unless a Bell company chooses to provide payphone service through an affiliate (rather than a unit of the Bell company itself) the payphone assets need not be transferred to unregulated books, the fair market value need not be assessed, and only the net book costs of the Bell companies' physical assets need be credited to regulated accounts. Order ¶¶ 162-164, 170-71.

v. United Food & Commercial Workers Union, Local 23, 484 U.S. 112, 123-30 (1987). When an agency ignores the Congressional intent plainly revealed by the legislative history and design of the statute, the Court should reverse the agency.

A. The Commission Has Failed To Follow A Clear Congressional Directive

In explaining Section 276(b)(1)(B)'s command to "discontinue . . . all payphone subsidies," the Conference Report unambiguously instructed the FCC to require that the Bell companies' payphone operations to be "transferred, at an appropriate valuation, from the regulated accounts associated with local exchange services to the [Bell companies'] unregulated books." Conference Report at 158 (emphasis added).

The Commission Order disregarded these specific Congressional instructions. The FCC declined to require the Bell companies to "transfer" their payphone operations to "unregulated books." Instead, the Commission allowed Bell companies to leave their payphone operations in regulated books.[8] Order ¶¶ 161-171.

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[8] The Commission's accounting treatment does provide for reassignment of payphone assets to nonregulated subaccounts within regulated books. However, this accounting treatment, under the Commission's practice, precludes any valuation of the Bell companies' payphone operations.

The Commission also failed to require "an appropriate valuation" of Bell companies' complete "payphone operations." Under the Commission's Order, unless a Bell company chooses to operate payphones through an affiliate, the Bell company is only required to credit regulated accounts with the net book cost of the physical payphone assets. No valuation is conducted, and intangibles such as location contracts and goodwill are not even considered - even though the Commission acknowledged that a proper market valuation would include those intangibles. Order ¶ 164.

B. The Conference Report Language Is Fully Consistent With The Text Of The Statute

The Commission believed it could not require a transfer and valuation of the Bell company's payphone operations without changing its cost allocation rules.[9] Preferring to avoid changing its rules, the Commission proffered two meritless

[9] Contrary to the Commission's finding, carrying out the Congressional intent would not "effectively eliminate [the Commission's] cost allocation rules from application to payphone operations." Order ¶ 170. Those rules already recognize that in certain circumstances -- which appear to apply here since payphone operations have few, if any, assets in common with regulated services -- carriers must use separate books and appraise the value of intracorporate asset transfers between regulated and nonregulated operations. 47 C.F.R. § 32.23(b), cited in Order ¶ 164. In any event, Section 276 required the Commission to make any rule changes necessary to carry out Congressional intent.

rationales for disregarding the Conference Report's statement of intent.

First, noting that Congress did not require the Bell companies to place their payphone operations in a separate affiliate, the Commission reasoned that "if Congress intended that there be a 'transfer', Congress would have required . . . separate affiliates . . . ." Order ¶ 170.[10]

This rationale confuses separate *affiliates* with separate *books*. The Conference Report's statement requiring a transfer to unregulated *books* is fully consistent with a decision not to require separate affiliates. Indeed, when the Commission originally deregulated customer premises equipment ("CPE") in the 1980s, it specifically required non-Bell LECs to transfer their payphone assets to separate, unregulated *books*, even though non-Bell LECs were not subject to a separate affiliate requirement. Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services (Second

[10] The FCC seemed to think that the Conference Report language referred to the *Senate* version of Section 276, which contained unenacted language directing the FCC to consider a separate affiliate requirement. Id. In fact, the Conference Report language referred to the House version of Section 276, which was enacted virtually without change.

Computer Inquiry), Fifth Report and Order, FCC 84-547, 49 Fed. Reg. 46,378 (Nov. 26, 1984) ("CPE Detariffing Order").[11]

Second, the Commission stated that requiring a transfer at market value to unregulated books would be inconsistent with the "Computer III"[12] rules referenced in Section 276(b)(1)(C). Order ¶¶ 169-170.

The claimed inconsistency does not exist. The Conference Report language and the Computer III reference relate to different provisions of Section 276. Section 276(b)(1)(B) requires the FCC to discontinue subsidies -- a one-time regulatory change that "terminates the current system of payphone regulation" once and for all. House Report at 88. The Conference Report language on transferring and valuing payphone operations addresses the implementation of this one-time change.

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11 The FCC's current cost allocation rules had not yet been adopted at the time of the CPE Detariffing Order. However, the CPE Detariffing Order clearly demonstrates that requiring the use of separate books is fully consistent with not requiring separate affiliates. The CPE Detariffing Order is particularly relevant since, in other sections of the Order, the Commission recognizes that the appropriate implementation of Section 276 is to reclassify Bell companies' payphones as CPE. Order ¶ 142.

12 Amendment of Section 64.702 of the Commission's Rules and Regulations, CC Docket No. 85-229, 104 FCC 2d 958 (1986) (subsequent history omitted) ("Computer III"). In Computer III, the Commission applied cost allocation rules and a variety of other "nonstructural safeguards" to Bell companies' provision of nonregulated "enhanced" or information services.

The reference to Computer III is found in the next provision, Section 276(b)(1)(C). That provision requires the Commission to adopt "nonstructural safeguards" that will apply prospectively to prevent future subsidies after the transfer to unregulated books has occurred.

Further, and in any event, Section 276(b)(1)(C)'s citation of Computer III provides only a minimum guideline for the Commission to follow in those instances where Congress has not specifically directed otherwise. The reference to Computer III in no way authorized the Commission to disregard the Conference Report's specific guidance on how to discontinue the existing system of payphone subsidies.

II. THE COMMISSION DISREGARDED THE CLEAR CONGRESSIONAL INTENT TO PROHIBIT THE BELL COMPANIES FROM DISCRIMINATING IN THE PROVISION OF ANY SERVICE

The Commission again disregarded clear Congressional intent when it decided that Bell companies are free to discriminate in favor of their payphone services when they provide nontariffed services -- such as installation and maintenance of equipment and wire, and billing and collection for payphone services -- or when they pay commissions for operator services. This decision simply contradicts the plain meaning of

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ATTACHMENT 3

COST APPORTIONMENT METHODOLOGY
Telecommunications Plant In-Service

USOA - Part 32 Account	Cost Pools	Cost Pool Apportionment Basis	Regulated/Nonregulated Apportionment Basis	Cost Definition	Comments
2232 Circuit Equipment *(Continued)*	Equal Access	Cost Pool Equals Subaccounts	Directly Assigned to Regulated	Directly Assignable	
	Network Reconfiguration	Cost Pool Equals Subaccounts	Directly Assigned to Regulated	Directly Assignable	
2311 Station Apparatus	Regulated	Not Applicable	Directly Assigned to Regulated	Directly Assignable	
	Nonregulated	Cost Pool Equals Account	Directly Assigned to Nonregulated	Directly Assignable	This account contains only nonregulated Station Apparatus Equipment investment.
2321 Customer Premises Wiring	Cost Pool Equals Account	______	Directly Assigned to Regulated	Directly Assignable	
2341 Large Private Branch Exchanges	Regulated	Not Applicable	Directly Assigned to Regulated	Directly Assignable	
	Nonregulated	Cost Pool Equals Account	Directly Assigned to Nonregulated	Directly Assignable	This account contains only nonregulated Large Private Branch Exchanges investment.
2351 Public Telephone Terminal Equipment	**Cost Pool Equals Account**	______	**Directly Assigned to Nonregulated**	**Directly Assignable**	Nonregulated Public Telephone Terminal Equipment associated with Ameritech's Inmate Services **is classified as nonregulated** pursuant to the Commission's Declaratory Ruling in RM-8181, Released February 20, 1996. **Other payphone equipment is classified as nonregulated pursuant to CC Docket No. 96-128, Released September 20, 1996.**
2362 Other Terminal Equipment	Cost Pool Equals Account	______	Directly Assigned to Regulated	Directly Assignable	
2411 Poles	Cost Pool Equals Account	______	Directly Assigned to Regulated	Directly Assignable	
2421 Aerial Cable	Cost Pool Equals Account	______	Directly Assigned to Regulated	Directly Assignable	
2422 Underground Cable	Cost Pool Equals Account	______	Directly Assigned to Regulated	Directly Assignable	
2423 Buried Cable	Cost Pool Equals Account	______	Directly Assigned to Regulated	Directly Assignable	

Cost Allocation Table

ACCOUNT	COST POOL NAME	COST POOL IDENTIFICATION BASIS	COST POOL ALLOCATION METHOD	COMMENTS
2231	Radio Systems - Paging -Directly Attributable Joint	Directly identifiable by Field Reporting Code, Equipment Category Number and Separations Suffix.	Peak forecast usage - Paging: number of subscribers per year	Associated with nonregulated features of Paging.
	Radio Systems -Directly Assigned Regulated	Residually identifiable by account.	Directly assigned to regulated.	Associated with tariffed/regulated services or a regulatory requirement (EA/NR).
	Radio Systems -Directly Assigned Nonregulated	Directly identifiable by Field Reporting Code.	Directly assigned to nonregulated.	
2232	Circuit Equipment -Directly Assigned Regulated	**Directly Identifiable by Field Reporting Code.**	Directly assigned to regulated.	Associated with tariffed/regulated services or a regulatory requirement (EA/NR).
	Circuit Equipment -Directly Assigned Nonregulated	Directly identifiable by Field Reporting Code.	Directly assigned to nonregulated.	
2311	Station Apparatus -Directly Assigned Regulated	N/A	Directly assigned to regulated.	Account and cost pool not in use.
	Station Apparatus -Directly Assigned Nonregulated	Cost pool equals account.	Directly assigned to nonregulated.	Account not in use in Pacific Bell. Account reserved for preemptively detariffed CPE if marketed directly by Pacific Bell.
2321	Customer Premises Wiring -Directly Assigned Regulated	Cost pool equals account.	Directly assigned to regulated.	Account 2321 contains embedded Inside Wire placed prior to 1/1/81 which is undergoing amortization. Embedded Inside Wire is regulated by definition.
2341	Large Private Branch Exchanges -Directly Assigned Regulated	N/A	Directly assigned to regulated.	Cost pool not in use.
	Large Private Branch Exchanges -Directly Assigned Nonregulated	Cost pool equals account.	Directly assigned to nonregulated.	Account is used only for preemptively detariffed CPE. At the present, account contains only Embedded Digital NCTE.
2351	Public Telephone Terminal Equipment -Directly Assigned Nonregulated	**Cost pool equals account.**	Directly assigned to nonregulated.	

USOA ACCOUNT	COST POOLS	BASIS FOR APPORTIONMENT TO COST POOLS	BASIS FOR ASSIGNMENT TO REG/NON REG	COMMENTS
2351 Public Telephone Terminal Equipment (Cont'd)	Nonregulated	This cost pool is formed by **direct reporting.**	Directly **assigned** to Nonregulated.	
2362 Other Terminal Equipment		The pools of this account are based on direct reporting to Field Reporting codes. These codes are the lowest level of required detail entered into the accounting systems, and permit aggregation of costs to very specific function- related cost pools. The total of the cost pools shown is equal to the total account.		
	2362 Nonregulated	This cost pool is formed by direct reporting.	Directly assigned to Nonregulated.	
	2362 Regulated	This cost pool is formed by direct reporting.	Directly assigned to Regulated.	